From the Desk of CIO

ANG KOK HENG
Chief Investment Officer
Phillip Capital Management Sdn Bhd

PhillipMutual
It's a Matter of Trust
PHILLIP MUTUAL BERHAD
Company No. (570409-K)
Tel: 603 2783 0300 | Fax: 603 2166 6417
Webpage: www.phillipmutual.com | E-mail: phillipmutual@poems.com.my

Goodbye 2021 but Not to Covid-19

While we are getting ready to bid farewell to the year 2021 but we cannot say goodbye to Covid-19 yet especially with the emergence of the highly infectious new Omicron variant in November. We have been expecting life and businesses to revert to new normal soon with more economies opening up. The expected strong recovery of the global economy has to scale back a little with rising infection from the new and highly contagious virus. This is an additional challenge on top of the other challenges such as rising inflation, high commodity prices, disruption in global shipping, US QE tapering, rising interest rates, confrontation between US and China, political transition and imminent general election domestically. The challenges sound extensive but we have experienced numerous market uncertainties in the past too. There is not a year where we can be certain of the future.

We will end the year in a week and the main disruption to the market this year continues to center on Covid-19 virus. The initial expectation was a temporary pandemic as in the past, especially after the discovery of vaccines by various companies. However, with the emergence of Delta variant and recently Omicron mutation, the virus has outlasted the previous similar virus-led epidemic or pandemic.

This has caused a third or fourth wave of infections emerged in many countries (see Exhibit 1). Nonetheless, so far, no extensive lock down has been re-imposed and we think the global economy will still record strong recovery growth, albeit at a slower pace.

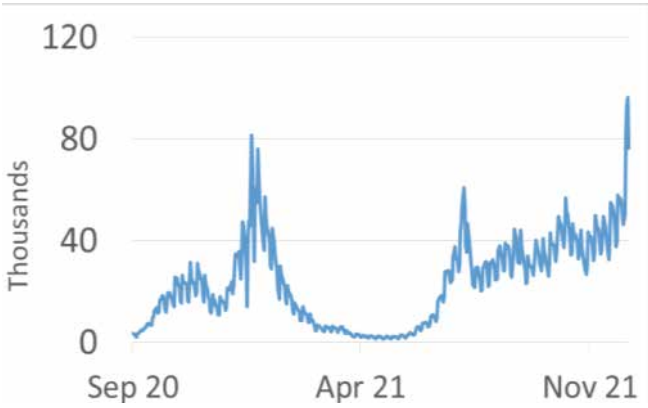
Other than the spillover of the pandemic into 2022, there are many other challenges ahead of us. Inflation, though high, will subside on a year-to-year basis as the base is now higher.

One of the biggest concerns is the expected tightening in the US following the strong economic recovery, plunging unemployment rate and strong retail sales. The US Fed (Federal Reserve) has indicated it will accelerate the reduction of bond purchase (or QE tapering) that will end March next year instead of July as initially planned. After that the Fed will raise its federal funds rate by three times instead of once in 2022 (see Exhibit 2) and another two or three hikes in 2023. That is the plan for now.

It is good that the US should unwind the huge liquidity expansion to counter the impact of pandemic i.e. to purchase bonds (printing money) and drop interest rates since the economy is recovering. The unwinding process should be gradual to avoid sending shock wave to the market. The recent Fed meeting indicates that the Fed recognises the stronger-than-expected economic recovery and has decided to hasten the speed of tapering and rate hikes.

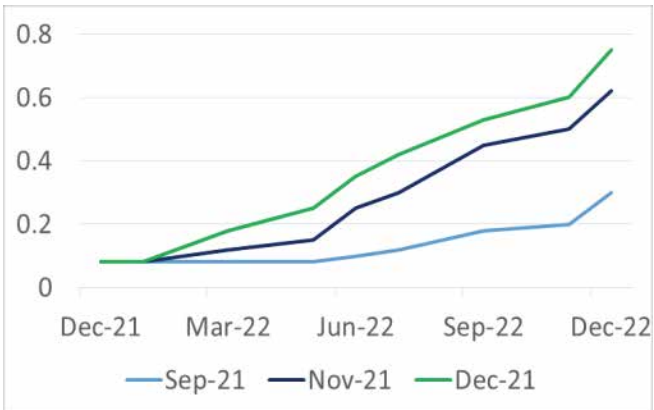
Nevertheless, the market seems to have shrugged off the tightening policy and digested the news well. Perhaps the market is now ready to accept the reality that the US interest rates cannot stay near zero forever. We still expect high market volatility in the coming year.

Exhibit 1: Covid-19 new wave in the UK



Source: gov.uk Dec2021

Exhibit 2: Expected rate hike in US



Source: Reuters, PCM, 25 Nov 2021